[Frequently Asked Questions]

Derivatives in the International Finance Market

Subject:	Business Economics
Course:	B. A. (Hons.), 6th Semester, Undergraduate
Paper No. & Title:	Paper – 611 International Finance
Unit No. & Title:	Unit – 2 Derivatives in the International Finance Market
Lecture No. & Title:	Lecture – 1 Derivatives in the International Finance Market

Frequently Asked Questions

Q1. What is a derivative?

A1. Derivatives are such types of contracts where the value of the asset is derived from the value of another asset.

Q2. What is an underlying asset?

A2. The asset on which the value of the derivative is derived is known as an underlying asset.

Q3. Which assets can be underlying assets?

A3. underlying asset can be share, stock market index, interest rate, commodity or currency.

Q4. Which derivatives provide protection to participants in financial markets against the adverse movements in the prices of the underlying asset?

A4. The financial derivatives provide protection to the participants in the financial markets against the adverse movements in the prices of the underlying asset.

Q5. What are the major types of derivatives?

A5. The major types of derivatives are:

1. Forwards; 2. Futures; 3. Options

Q6. What are Forward Contracts?

A6. Forward contracts are agreements made by two parties to exchange a specific amount of money for a particular asset at a predetermined future date.

Q7. Which are the parties involved in the forward contract?

A7. One of the parties under the agreement agrees to buy the underlying asset at a pre decided price. Such a party is known to assume a long position. On the other hand, another party agrees to sell the underlying asset at a pre decided price. Such a party is known to assume a short position.

Q8. Is there a counter-party risk in forward contract?

A8. Yes, there is a risk of counter party default in forward contract.

Q9. What are futures contracts?

A9. The futures contracts are standardised agreements where exchange of a specific type of asset for a specific amount is undertaken at a specified future date

Q10. What are options contracts?

A10. An option is such a type of derivative which gives the buyer a right to buy or sell the underlying asset at a predetermined rate on a future date without putting on him an obligation to do so.

Q11. What is Call Option?

A11. In Call Option, the buyer has a right to buy the underlying currency at a specified price and the seller or writer has the obligation to sell the Underlying currency (to the option holder) at the Specified price.

Q12. What is Put Option?

A12. In Put Option, the buyer has a right to sell the underlying currency at a specified price and the seller or writer has the obligation to buy the Underlying currency (from the option holder) at the Specified price